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SUBJECT: CHINA'S AMBITIOUS FREE TRADE AGREEMENT AGENDA FOR 2006

REFS: A) BEIJING 6453, B) BEIJING 6849, C) CANBERRA 1845, D) SANTIAGO 2322, E) WELLINGTON 366

11. (SBU) Summary: Chinese Ministry of Commerce (MOFCOM) Minister Bo Xilai announced in early 2006 an ambitious plan for nine free trade agreements (FTAs) covering twenty-seven countries, according to MOFCOM officials. These twenty-seven countries represent 18 percent of China's imports and 11 percent of Chinese exports, but the proposed agreements would not cover all traded goods. China's growing demand for raw materials, energy, and light manufactured goods to support its export-led growth is fueling the trade component of the PRC's broader "go out" policy. Preferring to engage first in relatively easy-to-win FTAs focusing only on goods, China is meeting resistance in negotiating FTAs with more developed countries. Trade in services and investment have been relegated to later stage negotiations except in the case of Australia, which is seeking a comprehensive FTA.

12. (SBU) Summary continued. China is implementing early stage trade agreements with ASEAN, Chile and Pakistan this

year. Negotiations with Australia, New Zealand and the Gulf Cooperation Council (GCC) are expected to conclude over the next one to two years. China is conducting feasibility studies with Iceland and South Africa. Paragraphs 8 - 20 summarize the status of FTAs. Comment follows. End Summary.

Overall Strategy Unclear but Easy FTAs Come First

¶3. (SBU) Asked to comment on press reports in early 2006 that indicated that Minister Bo planned to conclude nine FTAs covering twenty-seven countries, Ms. Wang Jingning, Deputy Director (Division II) of the Department of International Trade and Economic Affairs (DITEA) at MOFCOM confirmed that an ambitious FTA agenda exists. She clarified, however, that several of the previously announced bilateral negotiations have already concluded initial "Early Harvest" multi-round talks with tariff reductions being implemented this year. Two regional agreements (ASEAN and the Gulf Cooperation Council) cover sixteen countries. According to an Australian Embassy official based in Beijing, Australia has not set a timetable for concluding an FTA this year.

¶4. (SBU) While a focus on ASEAN is a strategic initiative for China's expansive trade agenda (the five ASEAN members accounted for 8 percent of total PRC trade in 2005), China has not announced plans for several countries that are large and growing trade partners (Brazil, India and Russia). Both Brazilian and Indian embassy officials based

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in Beijing have stated that FTA talks are highly unlikely in the near term. Countries that account for far smaller trade with China are actively engaged in negotiations (Chile, Pakistan and New Zealand). According to Ms. Zhang Bin, Deputy Director (Division I) of MOFCOM's DITEA, China's criteria for launching FTA negotiations are good political relations, an increasing trend in trade and a large potential market.

¶5. (SBU) Several Latin American diplomats based in Beijing have commented that the China-Chile FTA, which was negotiated relatively easily, is not an apt model for the rest of the region. These diplomats believe that it would be harder for their countries to agree on tariff reductions for Chinese products that would not hurt their domestic producers. DITEA's Zhang commented that Chile initiated talks on the FTA with China at an APEC meeting (see ref tel B). Since China's basic criteria were met, negotiations moved quickly.

China's FTA Negotiations Focusing on Goods

¶6. (SBU) China's recent FTA agreements have tended to focus on trade in goods followed by services and investment (e.g. Chile, ASEAN and GCC). According to MOFCOM officials, the goods component is most easily negotiated. Services and investment agreements, they contend, are more complicated and take longer to complete. The Australian FTA discussions, however, include goods, services, and investment (the outcome of arduous discussions according to an Australian diplomat based in Beijing). Australian officials are uncertain whether negotiations will in fact follow the Memorandum of Understanding guidelines established for the FTA talks with China (see para 16-18).

Organizational Limits on an Aggressive FTA Agenda

¶7. (SBU) According to Deputy Director Wang Jingning of MOFCOM DITEA Division II, two DITEA divisions with a staff of 20 persons are responsible for most FTA negotiations. Many of these 20 DITEA officials are relatively junior with

limited trade negotiating experience. Division One covers Chile, the GCC and Pakistan. Wang's division (Division Two) covers ASEAN and New Zealand. Because of limited DITEA staffing, responsibilities for FTA negotiations with Australia were shifted to MOFCOM's Department of WTO Affairs. (Note: The WTO Affairs Department was created at about the time of China's 2001 WTO accession and, at least initially, was largely staffed by officials formerly in DITEA. End note.) DITEA and the WTO Affairs Department both report to Vice Minister Yi Xiaozhun. Deputy Director

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Wang and her colleagues expressed strong interest in USG FTA talks with South Korea and in USG staffing size for FTA negotiation delegations and support.

Summary of FTA Agreements and Status

18. (U) Chinese FTA negotiators divide their negotiations into three phases. First the negotiators engage in "Early Harvest" talks that focus on tariff reductions on relatively non-controversial goods that can be implemented quickly. Recent Early Harvest agreements were launched and implemented within two years. The next phase is the launching of "Normal" negotiations which involve goods and services that require more effort. Lastly the negotiators tackle "Sensitive" track items which include the most contentious goods, services and investment sectors. According to Wang, the Chinese Government attempts to limit the number of goods placed on sensitive lists in FTA negotiations in two ways. First, the total value of sensitive items should not exceed ten percent of total goods traded bilaterally based on 2001 statistics. Second, the sensitive list should include no more than 500 items at the harmonized schedule (six-digit tariff line) level.

19. (SBU) Tariff reductions on a wide variety of goods with Chile, Pakistan, and ten countries in Southeast Asia (the ASEAN-5: Indonesia, Malaysia, Singapore, Thailand and the Philippines; CLMV: Cambodia, Laos, Myanmar, Vietnam; and Brunei) will come into effect in 2006. MOFCOM officials initially expected to conclude agreements in goods with New Zealand, Australia and the GCC by the end of 2006, but now believe it may take a bit longer. Chinese Premier Wen Jiabao recently announced that he expects an agreement with Australia in the next one to two years (see para 16-18). Wang stated that FTA feasibility studies are now underway with Iceland and South Africa. If the outcomes of the feasibility studies are positive, MOFCOM could begin "Early Harvest" negotiations within one year, Wang said.

ASEAN

110. (SBU) An Early Harvest Agreement on Trade in Goods was signed in November, 2004 with tariff reduction on 7,000 eight-digit tariff-line items beginning July, 2005. By 2010 ninety percent of tariffs are to be eliminated. Negotiations on trade in services and on investment are ongoing. This is the most significant Early Harvest Agreement China has concluded to date.

Chile

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111. (U) China and Chile signed an "Early Harvest" agreement in November, 2005 with tariff reductions to begin in July, 2006. Ninety-seven percent of tariffs are to be eliminated by 2015. Subsequent negotiations are expected. According to previous reporting (see reftel D) the FTA focused only on goods to accelerate conclusion of this agreement.

Pakistan

¶12. (U) Targeted tariff reductions on three thousand products began in April, 2006, one year after the "Early Harvest" Agreement was signed. Within two years 1,000 tariffs are to be eliminated entirely.

Hong Kong and Macau

¶13. (SBU) Ongoing discussions regarding trade liberalization continue. The mainland is interested in increasing tourism opportunities. No timeframe for formalization of agreements has been set, according to MOFCOM officials.

Gulf Cooperation Council (GCC)

¶14. (SBU) The GCC includes Saudi Arabia, United Arab Emirates, Kuwait, Bahrain, Oman, and Qatar. The UAE is the 2006 chair of the group which rotates yearly. Three trade negotiation rounds have been conducted as of early May 2006. Saudi Embassy Charge Maghrabi told Econoffs that he expects China and Saudi Arabia to conclude an agreement in goods only (no energy items) by the end of 2006. Mr. Cao Jiachang, Director in MOFCOM's West Asia Department, said the FTA talks with Saudi Arabia were progressing smoothly.

¶15. (SBU) The third round of negotiations was held in January, 2006 and covered custom inspections and sanitary and phytosanitary (SPS) trade remedies. Previous rounds were conducted in June, 2005 (trade and economy, investment protection, establishing a Joint Commission on Commerce and Trade) and April, 2005 (trade in goods, tariffs, intellectual property rights and technology transfer).

Australia

¶16. (SBU) According to an Australian embassy official in Beijing, Premier Wen's remarks during his recent visit to Australia regarding conclusion of an FTA within one to two years were encouraging. The Chinese and Australians are

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currently engaged in quarterly discussions on their FTA and thirty Australian negotiators are expected to arrive in Beijing on May 22nd for the fifth round of talks. Goals for this round include agreement on the text of the FTA.

¶17. (SBU) The Fourth Round, completed in Canberra in March, 2006, produced a Memorandum of Understanding for "comprehensive" negotiations including goods, services, and investments. This was the hardest point to come to agreement on, according to this Australian Embassy official, since the Chinese preferred to discuss only goods, leaving trade and investment to an unspecified time in the future. The Australian Government has not committed itself to a specific timetable. Based on Embassy Canberra reporting (see ref tel C) there is some doubt on the part of an Australian trade negotiator as to whether China will indeed follow through on a comprehensive negotiation.

¶18. (SBU) The March 2006 MOU established the completion date for the feasibility study period and also included Australian recognition of China's full market economy status. (Note: Australia thereby gave up seeking recourse to sections 15 and 16 of the Protocol of Accession of the PRC to the WTO and paragraph 242 of the WTO Report of the Working Party on the Accession of China. China has been pushing for this recognition, because it limits anti-dumping actions that can be initiated by its trade partners. End note.)

New Zealand

¶19. (SBU) According to the New Zealand Deputy Chief of Mission in Beijing, the fifth round of negotiations went well. The Chinese negotiating team was technically oriented and very interested in formalizing an agreement (See ref E for another account.) Trade in goods and intellectual property rights are the main issues being discussed. They are exploring establishment of a Joint Commission on Commerce and Trade (JCCT) similar to the USG's JCCT but are meeting resistance from the Chinese. New Zealand officials are under significant pressure from NZ businesses to have an IPR-related mechanism to resolve disputes, according to a New Zealand Embassy Economic Official.

Iceland and South Africa

¶20. (SBU) China has begun preliminary feasibility studies with no set timetable for Iceland and South Africa. Asked why these two countries with minimal trade relations would be chosen, DITEA Deputy Director Wang surmised that those

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countries had approached China, seeking more access to China's large and growing market.

Comment

¶21. (SBU) Comment: While China's historically large trading partners fall outside of Minister Bo's free trade agreement agenda for 2006, China is pursuing a steady trade liberalization plan. These early "wins" give the trade negotiating teams more experience on relatively easier agreements as they tentatively approach larger trade partners. Recent Chinese discussions with Russia, Brazil and India did not include formal FTA negotiations but rather laid the groundwork for future exchanges and formal dialogues. For China, the FTAs also offer more political dividends and fewer costs than pushing forward in multilateral fora like the WTO Doha Development Round multilateral trade liberalization negotiations. It is likely that China's attempts to negotiate future FTAs will be more difficult and will take longer than their earlier agreements. End Comment.

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